

SUBCOMMITTEE NO. 2

Agenda

S. Joseph Simitian, Chair
Dave Cogdill
Alan Lowenthal



Thursday, April 29, 2010
9:30 a.m. or Upon Adjournment of Session
Rose Ann Vuich Hearing Room (2040)

Consultant: Bryan Ehlers

<u>Item</u>	<u>Department</u>	<u>Page</u>
Various	AB 32 Implementation	2
3360	California Energy Commission	10
8660	California Public Utilities Commission	21
8570	Department of Food and Agriculture.....	34
3540	Department of Forestry and Fire Protection	37

Resources—Environmental Protection—Energy—Transportation

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Funding AB 32 Implementation

The California Global Warming Solutions Act of 2006 [AB 32, Nunez] requires the reduction of statewide greenhouse gas (GHG) emissions to 1990 levels by 2020—a 25 percent reduction over current levels. The bill designated the Air Resources Board (ARB) as the lead agency in addressing GHG emissions, including planning, regulatory, and enforcement efforts and set a timeline for completion of various actions, including the following:

- Adopt regulations by January 1, 2008, to require reporting and verification of statewide GHG emissions. *[Adopted on time in December 2007.]*
- Develop a plan by January 1, 2009, encompassing a set of measures that, taken together, would be a means by which the state could achieve its 2020 GHG reduction target. This plan is commonly referred to as the AB 32 Scoping Plan. *[Adopted on time in December 2008, with underlying economic analysis updated in March 2010.]*
- Adopt regulations by, and enforceable no later than, January 1, 2010, to implement “early action measures” to reduce GHG emissions. *[Nine early action measures adopted on time; three still under review by the Office of Administrative Law.]*
- Adopt additional regulations by January 1, 2011, to be enforceable January 1, 2012, to achieve the GHG emissions reductions goals established by AB 32. These additional regulations may include those for “market-based” compliance mechanisms, as defined in AB 32. *[Various regulations have been adopted, including those to reduce GHG emissions from (1) light-duty vehicles (the “Pavley regulations”) and (2) trucks used to haul goods at ports. Regulations currently under development would implement a renewable energy standard (previously discussed in Committee on March 18 with respect to the Renewable Portfolio Standard) and reduce GHG emissions from (1) natural gas transmission and distribution systems and (2) refrigerant systems. The ARB’s Scoping Plan also proposes the establishment of a cap-and-trade mechanism, and regulations are expected to be adopted by the end of 2010 in order to take effect in 2012.]*

Governor’s Budget and LAO Recommendation. The following is taken from a recent LAO report on AB 32 implementation and provides not only an overview of the AB 32 funding and the Governor’s 2010-11 budget proposals, but also the LAO’s recommendations going forward:

Funding for AB 32 Implementation

Majority of AB 32 Implementation Has Been Funded Through Special Fund Borrowing. From 2007–08 through 2009–10, AB 32 implementation has been funded primarily from special funds and bond funds. Over this period, total

funding has ranged from a low of \$30 million in 2007–08 to a high of \$48 million in 2009–10. The largest funding source by far has been the Air Pollution Control Fund, supported by \$84 million in various loans over a three-year period from the Beverage Container Recycling Fund and the Motor Vehicle Account. Statute requires that these loans be repaid, with interest, from revenues from a new AB 32 administrative fee (not yet established at the time the loans were made). We discuss this new fee in further detail below.

New Fee Will Now Be Primary Funding Source for AB 32 Implementation.

Assembly Bill 32 authorized ARB to assess a fee on GHG emitters that are subject to state regulation to pay the state's administrative costs for implementing the statute. The ARB has adopted such a fee, which will go into effect beginning in the budget year. The fee will be assessed on natural gas utilities, users, and pipeline owners and operators that distribute or use natural gas in California; producers and importers of gasoline and diesel fuels; refineries; cement manufacturers; retail providers and marketers of imported electricity; and facilities that burn coal.

For each of the first four years, the overall level of fee collections will be based on a calculation of (1) the total amount of funds needed to implement AB 32–related programs in that year and (2) the amount required annually to repay the special fund loans that supported the program in its early years. (Under the ARB's plan to repay the loan over four years, it will need to collect an additional \$27 million annually for the first three years and \$9 million in the fourth year.) Beginning in year five, the fee will be based primarily on the revenue needed to pay for the program's annual budget. The fee that is charged to any individual emitter will be based on the entity's overall emissions and the carbon intensity of the fuel source associated with those emissions. Invoices are to be sent to affected entities 30 days after the state budget is enacted. The revenues collected will be deposited into the Air Pollution Control Fund, and will be available upon appropriation by the Legislature.

Governor's Budget Proposal

Governor Proposes \$39 Million to Implement AB 32 in 2010–11. The Governor's budget includes \$39 million allocated to twelve departments for the purposes of implementing AB 32–related activities. The figure below summarizes, on a department-by-department basis (1) base budget expenditures, and proposed new expenditures; and (2) the current number of base budget positions and proposed new positions.

Largest Percentage of Funding Goes to ARB's AB 32 Programmatic Activities. As shown in Figure 1, while multiple departments have workload associated with AB 32 implementation, the bulk of this work is being conducted by ARB. The ARB has requested budget approval for 155 personnel-years and \$33 million for the continued implementation of the Scoping Plan. The ARB's

budget request for AB 32 implementation can be broken down into the following five activity areas:

Figure 1

AB 32–Related Activities in the 2010–11 Governor’s Budget

(Dollars in Thousands)

Budget Item	Department	2010–11 Base Funding		New Funding Proposed in 2010–11		Totals in 2010–11 Governor’s Budget	
		Amount	Positions	Amount	Positions	Amount	Positions
0555	Secretary for Environmental Protection	\$1,821	6.0	—	—	\$1,821	6.0
1760	Department of General Services	416	5.0	—	—	416	5.0
2240	Department of Housing and Community Development	—	—	\$54	0.5	54	0.5
3360	California Energy Commission	590	5.0	—	—	590	5.0
3500	Department of Resources Recycling and Recovery ^a	—	—	501	6.0	501	6.0
3540	Department of Forestry and Fire Protection	—	—	1,255	—	1,255	—
3760	State Coastal Conservancy	—	—	120	0.8	120	0.8
3860	Department of Water Resources	236	1.0	326	2.0	562	3.0
3900	Air Resources Board	32,932	155.0	—	—	32,932	155.0
3940	State Water Resources Control Board	—	—	535	2.0	535	2.0
4265	Department of Public Health	—	—	299	—	299	—
8570	Department of Food and Agriculture	—	—	309	1.0	309	1.0
Totals		\$35,995	172.0	\$3,399	12.3	\$39,394	184.3

^a Formerly the Integrated Waste Management Board. Note that 6 positions and \$501,000 shown for the 2010–11 fiscal year is the result of redirection that was originally approved for the 2009–10 fiscal year.

Development and Implementation of GHG Emission Reduction Measures in Scoping Plan—\$23 Million; 99 Personnel Years. The Scoping Plan’s GHG emission reduction approach includes developing regulations, incentive programs, voluntary actions, and public outreach programs. Figure 2 summarizes ARB’s allocation of 99 personnel years in the budget year among various activities related to the development and implementation of Scoping Plan measures. For the 13 of the 27 regulations described in the Scoping Plan that have already been adopted, ARB’s role will shift to implementation and

enforcement of these regulations. The ARB will continue working on the development of the balance of the regulations in the budget year.

Figure 2

Development and Implementation of Scoping Plan Measures

	ARB Positions
Fuel, Electricity, and Industrial Sectors	61
Major Activity:	
▪ Develop and implement the renewable electricity standard	
▪ Implementation of Low Carbon Fuel Standard	
Other Activities:	
▪ Develop and implement regulation to reduce sulfur hexafluoride emissions from gas-insulated electricity transmission and distribution equipment	
▪ Develop and implement energy efficiency audits for large industrial sources	
▪ Develop and implement mandatory commercial recycling	
▪ Develop and implement regulation to reduce greenhouse gases from natural gas transmission and distribution	
▪ Develop and implement regulation to reduce greenhouse gases from oil and gas production, processing and storage	
Mobile Sources	13
Major Activity:	
▪ Develop and implement new greenhouse gas emission standards for passenger cars and light trucks	
▪ Develop and implement amendments to the zero-emission vehicle regulation	
▪ Develop and implement regional greenhouse gas targets pursuant to Chapter 728, Statutes of 2008 (SB 375, Steinberg)	
Cross-Cutting	25
Major Activity:	
▪ Develop and implement the cap-and-trade regulation for greenhouse gases	
Other Activity:	
▪ Implement fee regulation	
Total	99

- **GHG Emission Inventory and Reporting—\$3.8 Million; 19 Personnel Years.** For the budget year, ARB plans to continue to update and maintain the California statewide GHG emission inventory, including an update of GHG emissions for the 2007 and 2008 calendar years. It will also continue to support the mandatory reporting of GHG emissions data to the state, including ensuring third-party verification of emissions data reports. In addition, it will begin development of compliance-based GHG emissions accounting protocols, which are necessary to comply with AB 32's requirements for verification and enforcement of emission reductions.
- **Applied Studies and Scientific Analysis—\$3.5 Million; Ten Personnel Years.** For the budget year, ARB staff will continue to evaluate the technological

feasibility and cost-effectiveness of GHG emission reduction measures, and ARB will continue to fund contracted research that supports AB 32 implementation and the state's long-term goal of 80 percent GHG reduction by 2050.

- **AB 32 Program Planning—\$1.8 Million; 12 Personnel Years.** For the budget year, ARB plans to continue to track and coordinate the development and implementation of the 72 measures in the Scoping Plan among multiple state, federal, and local agencies. This effort is intended to maintain consistency with the requirements of AB 32's regulatory mandates. Planned activities include coordinating the state's several energy entities to meet GHG goals; working with the local air districts on new federally mandated GHG permitting programs; coordinating with the U.S. Environmental Protection Agency on its mobile and stationary-source GHG programs; participating in the Western Climate Initiative activities; and providing policy support to technical staff working on GHG reduction regulations.
- **Support and Administration—\$1.6 Million; 15 Personnel Years.** For the budget year, these staff provide legal, legislative, information technology, and personnel-related support.

Evaluating the Budget for AB 32 Implementation

We do not have significant concerns with the overall level of AB 32-related expenditures proposed for the budget year. The department has generally provided sufficient workload justification for its requests. However, we are concerned that the board's budget may not provide sufficient funding for the board's economic analysis workload. We also are concerned that upcoming shifts in the nature of the AB 32 workload as a whole warrant careful budgetary planning. We discuss these two matters in more detail below.

Is Economic Analysis Underbudgeted? Current law prescribes multiple requirements for economic analyses as part of the regulatory adoption process. Such AB 32-related regulations as the Low Carbon Fuel Standard and the proposed cap-and-trade regulation can be particularly complex and break new regulatory ground, thereby making the required economic analysis challenging and labor-intensive. Our office and peer reviewers have raised concerns about the timeliness and the comprehensiveness of the ARB's economic analysis work connected with AB 32. A committee established to advise ARB on its analysis of the economic impacts of the AB 32 Scoping Plan voiced concern that insufficient ARB staff members and resources were available to analyze the potential economic impacts of AB 32.

Given these concerns, we recommend that the Legislature evaluate at budget hearings whether sufficient resources are being devoted by ARB to AB 32-related economic analysis work. To assist the Legislature in this evaluation, we recommend that ARB be directed to present at budget hearings (1) its projected AB 32-related economic analysis workload for the budget year, in terms of

required hours of staff time or contract resources, (2) the current level of staffing and other resources devoted to AB 32–related economic analysis, (3) the level of staffing and other resources it deems necessary to adequately address the projected workload, and (4) a plan to redirect resources from lower–priority activities to the extent that an unmet funding requirement for economic analysis is identified.

Ensuring That Future AB 32 Expenditures and Fee Levels Are Justified. The implementation of AB 32 will soon be at a major crossroads. Already in the fourth year of implementation, the program’s initial stage of planning, regulation development, and regulation adoption is nearing completion. (Regulations must generally be adopted by January 1, 2011.) The focus of the program will soon naturally shift from regulatory development to implementation and enforcement. As such, the “base budget” funding requirements for the program in future budget years could be substantially different than the program’s current funding requirements.

We believe that, beginning with the 2011–12 budget, the Legislature should step back and reevaluate the base funding requirements of AB 32 program implementation. In other words, the whole budget for AB 32 program implementation going forward after the budget year should be justified. This exercise will also be important from the perspective of ensuring that AB 32 administrative fees are set at an appropriate level to offset the costs of implementing the program.

Therefore, we recommend that the Legislature direct ARB to submit, as part of the 2011–12 Governor’s Budget, a zero–based budget and workload analysis for AB 32 program implementation across all state agencies in 2011–12. The administration should be directed to justify all expenditures proposed to support AB 32 implementation. This would enable the Legislature to better understand the overall size of the program and how funds are being allocated and prioritized for particular programs and functions, as well as how the proposed expenditures will further the goals and objectives of AB 32.

Staff Comments. Staff generally agrees with all of the issues raised by the LAO regarding AB 32 implementation. However, staff additionally notes the following concerns:

- 1) In developing the soon-to-be released cap-and-trade proposal, it is not clear that the ARB has yet met its statutory obligation to consider localized health impacts from air pollution.** Health and Safety Code 38570 reads in part:

(b) Prior to the inclusion of any market-based compliance mechanism in the regulations, to the extent feasible and in furtherance of achieving the

statewide greenhouse gas emissions limit, the state board shall do all of the following:

(1) Consider the potential for direct, indirect, and cumulative emission impacts from these mechanisms, including localized impacts in communities that are already adversely impacted by air pollution.

Staff notes that the Department of Public Health's (DPH) AB 32 proposal identified above (in Figure 1), requests resources to, among other things, "determine the co-benefits and/or unintended health consequences of various AB 32 mitigation measures, including the use of health impact assessments." Although the DPH proposal does not mention cap-and-trade specifically, the request raises concern that the ARB is proceeding, full-steam ahead, with development of cap-and-trade regulations without having adequately assessed the health impacts of such a mitigation approach. One example of the potential consequence of this is that the cap-and-trade regulations could systematically under- (or over-) value the benefit of localized GHG emissions (which are frequently accompanied by other emissions harmful to air quality and public health). The result could be that the proposed cap-and-trade system achieves less than optimal results by allowing/encouraging too many (or too few) emission reductions to be achieved out-of-state v. in-state. The Committee may wish the ARB to clarify its health-impact-assessment efforts to-date in relationship to the need for the requested DPH resources and the current roll-out date for the cap-and-trade regulations.

- 2) It is unclear how the nitrous oxide (N₂O) research proposed for funding under the California Department of Food and Agriculture (CDFA) would complement existing research efforts.** The ARB identified collaborative research of N₂O emissions from agricultural nitrogen applications (fertilizer) as number 31 on a list of forty-four early action GHG mitigation measures, and the ARB has signed off on the CDFA's request for one position and \$309,000 (supported by the AB 32 COI fee), including \$150,000 for external contracts, to conduct research and analysis on N₂O emissions emitted from California farmlands. However, staff notes that research on N₂O emissions from agriculture is already under way through the CDFA Fertilizing Materials Research and Education Program (FREP). While the CDFA indicates the proposed AB 32 resources would address "gaps" in the current research, it is not clear to staff whether: (a) such gaps exist and are meaningful in the overall AB 32 picture; and (b) assuming they are important gaps, whether permanent resources are necessary to address what would appear to be a limited-term workload (e.g., conducting a literature review of N₂O emissions research). The Committee may wish the ARB to clarify how the CDFA proposal fits within the broader AB 32 context, why it is a high-priority for funding at this time, and why it requires ongoing funding at this time.
- 3) Finally, there are AB 32-related activities that were previously identified in the "AB 32 Cross-Cut Budget" that are not being proposed for**

funding from the new Cost of Implementation fee. For example, the California Energy Commission has base funding of \$590,000 from the Energy Resources Programs Account that has been identified as AB 32-related. The Committee may wish to clarify whether these expenditures can or should be funded from the new fee (instead of a general surcharge on energy), and more generally whether each requested expenditure is proposed to be funded from a source with a proper nexus (e.g., only GHG mitigation—as opposed to global warming adaptation—efforts may be funded from the new fee).

Staff is prepared to recommend adoption of the LAO recommendation to require a zero-based AB 32 budget next year, but recommends the Committee hold this item open for the time being in order to allow the Administration an additional week to respond to the other concerns noted by the LAO and staff.

Staff Recommendation: HOLD OPEN.

3360 California Energy Commission

The Energy Resources Conservation and Development Commission (commonly referred to as the California Energy Commission or CEC) is responsible for forecasting energy supply and demand; developing and implementing energy conservation measures; conducting energy-related research and development programs; and siting major power plants.

Governor's Budget. The Governor's Budget includes \$420 million (no GF) for support of the CEC, a decrease of approximately \$366 million, due primarily to reduced federal fund expenditures (after a one-time influx of ARRA dollars in FY 2009-10).

[Discussion items begin on the following page.]

ITEMS PROPOSED FOR DISCUSSION

1. BCP-1: Augment Alternative and Renewable Fuel and Vehicle Technology Program. Chapter 750, Statutes of 2007 [AB 118, Nunez], created the Alternative and Renewable Fuel and Vehicle Technology Program (Program)—subsequently amended by Chapter 313, Statutes of 2008 [AB 109, Nunez]—authorizing the CEC to develop and deploy alternative and renewable fuels and advanced transportation technologies to help attain the state's climate change policies. The Program is supported by an annual \$10 million transfer from the Public Interest Research, Development, and Demonstration Fund, as well as annual revenues totaling about \$100 million from vehicle registration fees; identification plate fees; and vessel registration fees, which are deposited to the Alternative and Renewable Fuel and Vehicle Technology Fund (Fund).

The CEC has an annual program support budget of approximately \$100 million and provides financial support for projects that:

- Develop and improve alternative and renewable low-carbon fuels.
- Optimize alternative and renewable fuels for existing and developing engine technologies.
- Produce alternative and renewable low-carbon fuels in California.
- Decrease, on a full fuel cycle basis, the overall impact and carbon footprint of alternative and renewable fuels and increase sustainability.
- Expand fuel infrastructure, fueling stations, and equipment.
- Improve light-, medium-, and heavy-duty vehicle technologies.
- Retrofit medium- and heavy-duty on-road and non-road vehicle fleets.
- Expand infrastructure connected with existing fleets, public transit, and transportation corridors.
- Establish workforce training programs, conduct public education and promotion, and create technology centers.

Governor's Budget. The Governor requests a baseline increase of \$2 million from the (Fund) for contracts and technical assistance, including seeking to establish formal relationships with several national laboratories (approximately \$1.2 million); and a one-time augmentation of \$5 million for various projects.

Staff Comments. Each year the CEC must prepare and adopt a Program Investment Plan (Plan) that lays out its funding priorities and opportunities and describes how Program funding will be used to complement other public and private investments. The Plan is developed with the assistance of an advisory committee made up of representatives of fuel and vehicle technology consortia, labor organizations, environmental organizations, community-based justice and public health organizations, recreational boaters, consumer advocates, academic institutions, workforce training groups, and private industry; and representatives from the Resources Agency; the Business, Transportation and Housing Agency; the Labor and Workforce Development Agency; and the California Environmental Protection Agency. Staff notes that, by regulation, the adopted Plan can be adjusted during the year as the CEC sees fit.

Thus, legislative oversight of Program expenditures is somewhat limited by the fact that the investments/expenditures proposed at the time of Budget enactment are subject to change without consultation with or notification to the Legislature. That said, the budget process does offer the Legislature the opportunity to provide input regarding its priorities and adjust the overall Program spending (appropriation) authority as it sees fit. For example, staff notes that the 2009-10 Investment Plan initially allocated \$40 million for hydrogen fueling infrastructure; however, the Legislature raised concerns during the budget process about the efficacy of these expenditures and the amount was subsequently reduced to \$22 million.

AB 118 Draft Funding Allocation Summary for FY 2010-2011

Project/Activity	Purpose	Funding Allocation for FY (2010-2011)
Electric Drive	Develop and demonstrate advanced on-road and non-road medium- and heavy-duty vehicles	\$14 Million
	Infrastructure and related activities	\$3 Million
	Manufacturing facilities and equipment	\$7.5 Million
	Subtotal	\$24.5 Million
Hydrogen	Fueling Infrastructure	\$14 Million
	Subtotal	\$14 Million
Gasoline Substitutes	Expansion of E-85 dispensers and retail outlets	\$8.5 Million
	Gasoline substitutes production	\$10 Million
	Subtotal	\$18.5 Million
Diesel Substitutes	Diesel substitutes production	\$5 Million
	Bulk terminal storage and blending facilities	\$5 Million
	Subtotal	\$10 Million
Natural Gas	Medium- and heavy-duty vehicles	\$12 Million
	Upgrades to natural gas fueling stations	\$2 Million
	Biomethane production plants and quality testing	\$10 Million
	Subtotal	\$24 Million
Propane	Light- and medium-duty vehicles	\$3 Million
	Subtotal	\$3 Million
Innovative Technologies and Advanced Fuels	Innovative technologies and advanced fuels	\$3 Million
	Subtotal	\$3 Million
Market and Program Development	Sustainability studies	\$2.5 Million
	Program marketing and public education and outreach	\$2.5 Million
	Technical assistance and environmental/market/ technology analyses	\$6 Million
	Subtotal	\$11 Million
	Grand Total	\$108 Million

Based on the above, the Committee may wish to ask some, or all, of the following questions:

- Why is industry education and outreach necessary given the very high profile of alternative fuel and vehicle technology energy efforts in California? What kind of return on investment does the CEC expect on the proposed \$2.5 million expenditure for this purpose?
- The CEC proposes \$8.5 million for expansion of E-85 (ethanol) dispensers and outlets. Is not this just a subsidy to corn producers (who supply the vast majority of the inputs for California ethanol)? Notwithstanding the reduced emissions of blending Midwestern corn ethanol in California (rather than in the Midwest where coal is more frequently used for the power supply), why does this proposed investment make sense economically and environmentally when corn ethanol requires seven times the fossil fuel input per unit of energy as sugar cane ethanol?
- The CEC proposes \$14 million for hydrogen infrastructure to support "hydrogen highway" infrastructure—a proposal of which the Legislature disapproved last year. The draft Investment Plan shows fewer than 100 hydrogen fuel cell vehicles (FCVs) were on the roads in California's major metropolitan areas and "theoretical" price tags ranged into the millions of dollars. Granted, this Program is intended to "push" development of future technologies, and hydrogen may eventually pan out, why does it make sense to spend nearly 13 percent of the budget on hydrogen when other technologies are more "ready for prime time" and could produce greater bang-for-the-buck in the short-term?
- The CEC more than doubled funding to biomethane in updates to the current Investment Plan (for a total of \$21.5 million), and is proposing another \$10 million in funding in the new draft Plan. Could you please explain why we are subsidizing, or at least giving preferential treatment to, biomethane when it creates pollution and there are other options to reduce or reuse waste? (Staff notes that state policy is to promote waste reduction, recycling and composting, and only to burn or cook waste that cannot feasibly be managed in one of these more preferable ways.)

Given ongoing concerns and questions raised above, and the fact that the draft 2010-11 Investment Plan is set to be reviewed by the Advisory Committee on April 30, 2010, the Committee may wish to leave this item open for at least another week (or two) of review before determining whether to fully fund not only the requested augmentations but the \$100 million base Program.

Staff Recommendation: HOLD OPEN.

2. BCP-2: Distribution System Infrastructure Analysis to Support Integration and Use of Low Carbon Resources. Combined heat and power (CHP) technologies produce both electricity and steam from a single fuel at a facility located near the consumer, and, by recovering heat that normally would be waste in an electricity generator, save the fuel that would otherwise be used to produce heat or steam in a separate unit. Chapter 713, Statutes of 2007 [AB 1613, Blakeslee], the Waste Heat and Carbon Reduction Act, helped ensure a market for CHP and required the CEC to adopt the guidelines for various applications of combined heat and power systems that reduce waste energy.

Historically, central stations generated the power required by the state and transmitted the electricity at high voltage across the main transmission grid, through substations, where voltage was “stepped down” (i.e., reduced) for transmission to customers via lower voltage distribution system lines. Generally speaking, electrons only flowed one direction—from the power plant to the consumer. However, the push to develop a cleaner, more efficient, and more flexible energy system has resulted in a new focus on a number of areas, including: (1) CHP; (2) distributed renewable generation (smaller projects—like roof-topic solar installations—that are directly connected to the grid); and (3) the re-design of the electricity grid so that electrons (and information about their availability and demand) are able to flow freely to and from consumers/generators as needed (resulting in a “smart grid” that is constantly monitoring power supply and demand and allocating electricity in an optimal and reliable fashion—no unnecessary generation, and no unmet demand).

Governor’s Budget. The Governor requests the 2 two-year limited-term positions and \$282,000 (Energy Resources Program Account—ERPA) originally authorized to support adoption of the AB 1613 guidelines be made permanent. The positions would conduct ongoing oversight and management of the CHP program, but would also address distributed generation (DG) issues associated with developing a “smart grid” (e.g., determining where on the distribution system new generation provides value).

Staff Comments. According to the CEC, the requested positions are necessary to continue maintenance of the AB 1613 guidelines and to implement smart grid technologies. Among other things, the positions would:

- CHP – Maintain CHP guidelines. Develop methods for collecting and analyzing CHP data for use in forecasts and assessments to help the ARB assess progress toward meeting CHP goals associated with the AB 32 *Climate Change Scoping Plan*. Monitor and verify compliance based on annual reports provided by CHP facilities. Provide technical support to the PUC and ARB for rulemakings and proceedings.
- DG/Smart Grid – Model and plan how to best optimize the use of additional DG, as well as other non-traditional generation such as CHP. This would include: (1) determining where on the grid new generation would provide value; (2) identifying the infrastructure upgrades and new standards that will support smart

grid capabilities; and (3) review and comment on smart grid implementation plans and strategies.

Strictly speaking, AB 1613 requires very minimal staff work from the CEC on an ongoing basis now that program guidelines are in place. Furthermore, the CHP program created under AB 1613 is voluntary and it is not yet known how many (if any) businesses will take advantage. Therefore, to the extent that the CEC partially justifies the need for these two positions using AB 1613, that justification is weak.

Insofar as the CEC further justifies the need for these positions based on workload associated with DG and related smart grid development, staff notes concern that these are not activities the Legislature has directed the CEC to carry out (however beneficial they may be). Additionally, it is unclear the degree to which they may overlap with smart grid activities identified in Item 4 (below) that the CEC believes are necessary to implement Chapter 327, Statutes of 2009 [SB 17, Padilla]. As such, staff cannot support approval of this request at this time. If the Committee does not decide to deny the request outright, it may wish the CEC to identify the relevant statutory references requiring the CEC to undertake the identified activities, and to work with staff to clarify the difference between this proposal and the SB 17 request.

Staff Recommendation: HOLD OPEN.

3. BCP-3: Energy Efficiency Program for Existing Residential and Nonresidential Buildings (Implement AB 758). State energy policy prioritizes energy efficiency measures (e.g., replacing incandescent light bulbs with compact fluorescent ones) to reduce energy usage because efficiency strategies generally provide a bigger “bang for the buck” (in terms of energy savings) than investment in infrastructure.

Approximately 60 percent of California’s existing residential building stock, and around 45 percent of non-residential stock, was constructed before the state established energy efficiency standards for new buildings in 1978. Therefore, there are likely significant energy savings to be had by improving the energy efficiency of these buildings.

Chapter 470, Statutes of 2009 [AB 758, Skinner and Bass], requires the CEC to develop and implement (through regulations) a comprehensive program to achieve greater energy savings in existing residential and nonresidential building stock, including energy assessments, cost-effective energy efficiency improvements, financing options, public outreach, and education efforts.

Governor’s Budget. The Governor requests ten permanent positions and \$1.8 million (federal funds), including \$500,000 for contract expenses, to implement AB 758. The proposed federal funds would come from American Reinvestment and Recovery Act (ARRA) dollars for the State Energy Program (SEP) in FY 2010-11, but costs would begin to shift to the ERPA in FY 2011-12, and would be entirely borne by the ERPA beginning in FY 2012-13.

Staff Comments. The CEC has temporarily redirected staff to begin the start-up work required to implement AB 758, including opening of the rulemaking proceeding (which took place in February 2010). Additionally, the CEC has requested the United States Department of Energy to approve an amendment to its ARRA SEP grant application that would authorize the use of ARRA SEP monies, from the \$15 million currently identified for Program Support and Contracts, for AB 758 purposes.

Staff notes that neither the BCP, nor the CEC’s public website, nor materials provided in multiple hearings before the budget and policy committees this year indicated that the ARRA SEP Program Support and Contracts monies would be used for this purpose. While AB 758 specifically instructed the CEC to use ARRA funds for this purpose, the CEC could have, and should have, been more transparent about which “pot” of funding it intended to use. At it stands, this episode raises some question about how other Program Support and Contracts funds are to be spent and the Committee may wish the CEC to provide additional detail (not only to legislative staff, but to the public via the CEC website).

As to the requirements of the bill and the justification for the requested resources, staff notes that this proposal is consistent with the legislative fiscal analysis of the bill. However, there remains some dispute over whether or not the bill permits the program to be supported by state funds—as noted above, the Administration proposes to use

ERPA funds in the out-years once ARRA dollars are exhausted. The language in question reads as follows:

The commission shall fund activities undertaken pursuant to this section from the Federal Trust Fund consistent with the federal American Recovery and Reinvestment Act of 2009 (Public Law 111-5) or other sources of nonstate funds available to the commission for the purposes of this section.

Staff notes that the word “only” (which immediately preceded “fund”) was deleted from an earlier version of the bill, in order, presumably, to make use of ERPA (or other state funds) legal. However, to the extent that existing statute remains unclear (in that use of state funds is not explicitly authorized) there is room for alternate interpretations and/or legal challenge. Thus, the Committee may wish to consider: (1) a clarifying amendment to the statute; and/or (2) opting to fund only the development of the program (which would require significantly fewer resources than proposed), and defer the decision to fund program implementation until a later date when a future source of non-ARRA funds, that is clearly legal, is identified.

Staff Recommendation. HOLD OPEN for the time being and direct the CEC and DOF to work with staff and LAO to develop a refined estimate of the resources necessary to develop the program (rather than develop and implement it).

4. BCP-4: Smart Grid Development (Implement SB 17). As discussed briefly in Item 2 (above), the term “smart grid” refers to an electricity distribution system that allows for the flow of information (and electrons) in two directions—recognizing that with DG, traditional “customers” will increasingly become energy suppliers. Through this modernization of the grid, the goal is to increase efficiency, reliability, and flexibility of the system, and reduce the rate at which additional electric utility infrastructure needs to be built. A smart grid is a key element to the greening of California’s electrical system due to the intermittent nature of renewable electricity resources such as wind and solar.

Chapter 327, Statutes of 2009 [SB 17, Padilla] established the smart grid policy for the state and requires the following:

- The PUC, *in consultation with* the CEC and the Independent System Operator (ISO), to determine the requirements for a smart grid deployment plan, consistent with state and federal law, no later than July 1, 2010.
- Electrical corporations, by July 1, 2011, to develop and submit a smart grid deployment plan to the PUC for approval.
- The PUC, *in consultation with* the CEC, the ISO, and electrical corporations, at each step of deployment, to evaluate the impact of deployment on major initiatives and policies.
- Each Publicly-Owned Utility (POU) to develop by July 1, 2011, a smart grid deployment plan consistent with federal law.

Governor’s Budget. The Governor requests two permanent positions and \$287,000 (ERPA), to provide the PUC with consultation on defining and developing a smart grid in California.

Staff Comments. As the CEC’s role under SB 17 was intended to be merely consultative, the Senate fiscal analysis estimated costs of only \$100,000 annually (from the Public Interest Research, Development, and Demonstration Fund—PIRDDF). However, based on this request (for nearly triple the originally estimated resources) and conversations with CEC staff, it is clear that the CEC sees a larger role for itself in SB 17-implementation particularly with regard to the POUs. As staff does not necessarily see an explicit role for the CEC in developing smart grid plans at the POUs (this is a federal mandate), the likely recommendation would be to deny all but \$100,000 and one position from this request. However, the Committee may wish to have the CEC further explain its rationale for additional resources (and for the use of the ERPA, as opposed to the PIRDDF).

Staff Recommendation: HOLD OPEN.

5. FL: Augment Siting Program and Renewable Energy Development Support (TBL). The CEC's Siting, Transmission, and Environmental Protection Division (Division) licenses thermal power plants of 50 megawatts (MW) or more, as well as associated transmission line infrastructure, fuel supply lines, and other related facilities. As such, the Division must ensure compliance with the Warren-Alquist Act (which authorized the CEC) and the California Environmental Quality Act (CEQA).

Beginning in the aftermath of the 2000-01 state energy crisis, and accelerating with the adoption of the Renewable Portfolio Standard (RPS), siting applications for new electricity generation in California have increased dramatically over the last number of years. For example, since 1999, the CEC has approved 68 projects, more than double the number of projects approved in the preceding 25 years. According to the CEC, the current siting workload is four times higher than the historic average, 26 projects under active review, of which 15 are traditional natural gas-fired power plants and 11 are solar thermal power plants. In addition, the CEC is also reviewing two major amendments to existing licenses, and it expects to receive another six to eight power plant applications over the next six months alone.

Governor's Budget. The Governor requests nine positions and a two-year total of \$8.7 million—\$6.2 million in FY 2010-11—from the Energy Facility License and Compliance Fund to process electricity generation siting applications and to ensure the more rapid development of the Desert Renewable Energy Conservation Plan (DRECP). Of the requested amount, \$5.2 million in FY 2010-11 and \$3.8 million in FY 2011-12 would go to continued funding of a peak siting workload contract (valued at \$6.2 million in the current fiscal year).

Additionally, the Governor requests trailer bill language (TBL) to increase existing licensing fees and expand them to include renewable generation. The proposed increases include raising: (1) the standard fee from \$100,000 to \$250,000; 2) the per-megawatt fee from \$250 to \$500; and 3) the fee cap from \$350,000 to \$750,000.

Staff Comments. Last year the Legislature approved a total of \$5.1 million and 28.5 positions to address increased Siting Division workload. However, historically, noncompetitive salaries have made certain siting positions difficult for the CEC to fill and retain. So, more recently, Chapter 9, Statutes of 2010, Eighth Extraordinary Session [SBx8 34, Padilla] provided the CEC to pay recruitment and retention differentials to certain employees working in the Division. While CEC staff indicate the new differentials provided a significant boost to morale, and will hopefully lead to improved recruitment and retention (it is somewhat early to gauge the impact), the Division remains highly dependent upon contracted staff to address the current historic peak workload. Furthermore, the CEC expects these high-priced contract staff will be necessary for some years to come as siting applications can take many years to process. Thus, while the CEC deems it appropriate to continue using some contracts (rather than hire permanent staff to address workload that is not ongoing), it requests additional state staff to provide: (1) adequate oversight of the contracted help; and (2)

best value to the state by supplanting more costly contractors with less costly state personnel (where long-term workload justifies additional permanent staff).

While the Division hired twenty new staff in Fall 2009, filling most of the newly approved positions, there remain 18 Division vacancies, including seven (out of 50) Planners—the journey-level classification for licensing workload. CEC staff indicate that they are currently working with a contractor and the Department of Personnel Administration to develop a new classification structure for the entire CEC that will help to address the recruitment and retention problems in the Planner series classifications. However, in the meantime, while it is generally more economical to use civil service employees than to employ contractors, the current heavy workload has constrained the CEC's ability to train new staff, and thus the number of additional staff added at this particular time must be curtailed to take this into account. Even so, the Committee may wish to inquire as to why the CEC is not looking to focus more on adding supervisory-level positions in order to ensure that there is adequate oversight of contracted work and to prevent bottlenecks in the siting approval process.

With regard to the requested TBL, staff notes that the CEC proposal is largely consistent with the LAO recommendation to delete the existing fee-exemption for renewable projects. While originally intended to encourage development of renewable generation, the CEC estimates that the fee-exemption has resulted in foregone revenue to the Division of \$3.3 million since the end of 2007, at a time when the Division is unable to meet statutory application-processing deadlines due to lack of resources. Furthermore, the LAO points out that, viewed from the standpoint of the beneficiary pays principle, the fact that ratepayers support 88 percent of the Division's costs is inequitable. While the proposed fee changes would bring about more parity between the ratepayers and developers/operators in terms of supporting the Division's costs, staff notes that it would not achieve a 50/50 split (as might be deemed equitable). DOF staff have indicated that the Administration intends to monitor the effect of the fee changes on developer/operator behavior (in order to make sure that the changes do not actually result in decreased revenue), but intends to move toward a 50/50 cost-allocation in the future. Staff would only point out that the current Administration will leave office in November and there is great uncertainty about whether a future Governor will follow through on this commitment. Thus, the Committee may wish to determine what fee level would achieve parity between ratepayers and developers/operators and weigh the benefits versus the risks of enacting higher fees now.

Staff Recommendation: HOLD OPEN.

8660 California Public Utilities Commission

The California Public Utilities Commission (PUC) is responsible for the regulation of privately owned "public utilities," such as gas, electric, telephone, and railroad corporations, as well as certain video providers and passenger and household goods carriers. The PUC's primary objective is to ensure adequate facilities and services for the public at equitable and reasonable rates. The PUC also promotes energy conservation through its various regulatory decisions.

Governor's Budget. The Governor's Budget proposes \$1.2 billion to support the CPUC in the budget year. This is approximately \$150 million less than estimated expenditures in the current year. This is due to a large reduction in the California High-Cost Fund B Administrative Committee Fund, a special fund. The commission does not receive any General Fund support.

Governor's Budget. The Governor's Budget includes \$1.4 billion (no GF) for support of the PUC, an increase of roughly \$200 million over current year expenditures, due primarily to an increase in the Universal Lifeline Telephone Service Trust Administrative Committee Fund.

ITEMS PROPOSED FOR VOTE-ONLY

1. BCP-2: Increase Compliance Audits of Utility Procurement Activities (Focus on Day-Ahead and Hour-Ahead Transactions). The Governor requests one position and \$85,000 from the PUC Utilities Reimbursement Account (PUCURA) to better evaluate the utilities' compliance with procurement rules for electric resources. Specifically, the PUC proposes to increase audits from less than 0.5 percent of quarterly transactions to approximately one percent, with a focus on the millions of dollars spent on day-ahead and hour-ahead transactions.

2. BCP-5 Rail Transit Safety Oversight. The Governor requests three positions and \$312,000 (Public Transportation Account, State Transportation Fund) for increased rail transit safety oversight, including: (1) better tracking of corrective action plans; (2) additional inspections of 12 existing rail transit systems and the dozens of new construction projects underway at any given time.

3. BCP-6: Pilot Test and Survey of Limited English Proficiency (LEP) Communications Customers. The Governor requests \$2.3 million (reimbursement authority) to conduct a customer satisfaction survey of limited English proficient customers of California communications utilities relative to the general English proficient population. A pilot may be conducted to develop sample design parameters from a limited number of customers in order to determine final design parameters for the survey, which will then be administered over the remainder of a two-year period to approximately 15,000 LEP customers. Carriers with \$10 million or more in annual intrastate revenue are ordered to provide reimbursement on a prorated basis.

4. BCP-9: Centralized Fines and Restitution Collections (Make Permanent Limited-Term Positions). The Governor requests three limited-term positions and \$162,000 (various special funds) originally approved in FY 2008-09 be made permanent in order to continue a pilot program for centralized fines and restitution collections. The pilot program was initiated in response to a State Controller's Office audit recommendation to address an internal control weakness.

5. BCP-10: Modernize Elevators at PUC Headquarters. The Governor requests a one-time augmentation of \$2.2 million (various special funds) to modernize seven 23-year old elevators in the PUC headquarters building. PUC staff indicate that problems with the elevators resulted in over 150 calls last year, resulting in costs in excess of \$25,000, and a consultant study (previously approved by the Legislature) determined that, while the elevators have an expected 30-year useful life, \$2.2 million in modernizations (e.g., install new motors) are required.

6. BCP-13: Comprehensive Energy Efficiency Residential and Non-Residential Programs (Implement AB 758). The Governor requests one position and \$112,000 (PUCURA) to implement Chapter 470, Statutes of 2009 [AB 758, Skinner and Bass]. AB 758 requires the CEC, in consultation with the PUC, to develop and implement (through regulations) a comprehensive program to achieve greater energy savings in existing residential and nonresidential building stock, including energy assessments, cost-effective energy efficiency improvements, financing options, public outreach, and education efforts.

7. BCP-14: Establish Net Surplus Compensation for Solar and Wind Distributed Generation (DG) Net Energy Metering Customers (Implement AB 920). The Governor requests 2.3 positions (including 0.3 one-year Administrative Law Judge) and \$242,000 (PUCURA) to conduct a ratemaking proceeding and ongoing program monitoring for a new Net Surplus Compensation Program, pursuant to Chapter 376, Statutes of 2009 [AB 920, Huffman], that would allow customers on Net Energy Metering tariffs to sell excess electricity to their electric utility after certain conditions are met.

8. FL: Technical Adjustment—Align Lease Revenue Bond Payments with Programs Housed in Main Headquarters Building. The Governor requests deletion of Items 8660-003-0412 and 8660-003-0461 and a corresponding increase of \$712,000 in Item 8660-003-0462 to reflect the relocation of Commission staff regulating transportation from the PUC headquarters building (meaning the funds that support these activities will no longer be billed for lease revenue bond payments on the headquarters facility).

9. BCP-7: Division of Ratepayer Advocate (DRA) – Energy Efficiency Programs and Activities. The Governor requests one position and \$96,000 (PUC Ratepayer Advocate Account) to ensure investor-owned utility energy efficiency programs are cost-effective for ratepayers. The DRA indicates that the approved 2010-12 energy

efficiency program budget for the four largest energy utilities is \$3.1 billion, a 61 percent increase in ratepayer investments over the previous cycle. The requested position would augment the two DRA positions currently assigned to energy efficiency program monitoring.

10.BCP-8: DRA – Energy Low Income Assistance Programs & Activities. The Governor requests one position and \$95,000 (PUC Ratepayer Advocate Account) to address expanding workload on energy low income assistance programs and activities, including the California Alternative Rates for Energy (CARE) program, the Low Income Energy Efficiency (LIEE) program, and a new rulemaking on the adoption of regulation related to arrearage management and shut-off prevention for residential customers of electricity and natural gas utilities. With nearly five million California energy customers projected to be low income by 2012, and utility investments in the above programs growing (e.g., CARE expenditures by the four largest utilities increased from \$126 million to \$818 million from 2001 to 2008), the DRA indicates the one position currently assigned to monitor these activities is insufficient to adequately serve ratepayers.

Staff Recommendation (for Vote-Only Items 1-10): APPROVE Items 1-8 listed above, but HOLD OPEN Items 9 and 10 due to questions from the Chair.

VOTE:

ITEMS PROPOSED FOR DISCUSSION

1. BCP-1: Renewable Portfolio Standard (RPS) and Renewable Transmission. As discussed on March 18, 2010, when this Committee heard a similar item related to the Air Resources Board (ARB), though in conceptual agreement on a 33-percent RPS, the Governor and the Legislature remain at odds over how best to implement such a standard, and the Governor has plunged ahead, ordering the Administration to implement a 33-percent standard in the absence of legislative approval.

The LAO included the RPS issue in its *Analysis of the 2010-11 Budget Bill*, and the following is the bulk of the LAO's write-up with some staff edits for brevity:

Current RPS Law

RPS Standard Now Set at 20 Percent. Current law, as amended in 2006, requires each privately owned electric utility to increase its share of electricity generated from eligible renewable energy resources by at least one percent each year so that, by the end of 2010, 20 percent of its electricity comes from renewable sources.

Enforcing the RPS. Current law requires the California Public Utilities Commission (CPUC) to enforce compliance by the private utilities (commonly referred to as investor-owned utilities, or IOUs) with the 20 percent RPS. The CPUC is prohibited from ordering an IOU to procure more than 20 percent of its retail sales of electricity from eligible renewable energy resources.

Vetoed 2009 RPS Legislation. During the 2009 legislative session, the Legislature passed, and the Governor subsequently vetoed, a package of RPS-related bills. These bills—which included SB 14 (Simitian), AB 21 (Krekorian), and AB 64 (Krekorian)—together would have increased the RPS target for IOUs to 33 percent by 2020 and also made publicly owned utilities subject to the same RPS targets as these other electricity providers. In his veto messages, the Governor cited his policy concerns about the Legislature's approach to meeting a 33 percent RPS, a target which he nonetheless supported.

Administration's Recent RPS Activity Circumvents Legislative Authority

As discussed below, our review finds that over the last few years, the administration has been involved in a number of activities that, in effect, circumvent the Legislature's policy direction as reflected in current RPS law.

Governor's Two Executive Orders. In November 2008, the Governor issued an executive order calling for *all* providers of retail electricity (thereby including publicly owned utilities) to obtain 33 percent of their electricity from renewable sources by 2020. State government agencies were directed to "take all appropriate actions" to implement this target. In September 2009, after vetoing legislation that would have placed a 33 percent RPS target in statute, the Governor issued another executive order directing ARB to develop a regulation

“consistent with” a 33 percent renewable energy target. The executive order indicated that the administration believed that it had the legal authority to establish such regulations under the Global Warming Solutions Act of 2006 (commonly referred to as “AB 32”). The ARB currently is working to develop this regulation.

Executive Orders Cannot Replace or Circumvent Lawmaking. In a recent written opinion, the Legislative Counsel advised us that, as a general proposition, the Governor may not issue an executive order that has the effect of enacting, enlarging, or limiting legislation. In the context of the Governor’s September 2009 executive order, we are advised that the ARB may not adopt a renewable energy–related regulation that contravenes, changes, or replaces the statutory requirements of the current RPS law. According to Legislative Counsel, AB 32 does not authorize the ARB to adopt such a regulation. Since current RPS law is very prescriptive in its requirements, this prohibition would severely constrain the ARB in developing its regulation pursuant to the executive order. For example, we are advised by Legislative Counsel that the ARB could not develop a regulation that contravenes the current–law prohibition upon requiring an IOU to procure more than 20 percent of its electricity from renewable sources. Given this legal opinion, in our view it would clearly be inappropriate for the administration to circumvent the existing RPS law by attempting to implement a new renewable energy standard on its own authority.

Planning Activities. Despite these legal constraints, the administration has been involved in various planning activities that assume an RPS target that is different than the one established in current law. For example:

- The ARB’s plan to implement AB 32 (commonly referred to as the AB 32 Scoping Plan) includes a 33 percent RPS as one of its primary measures to achieve the state’s greenhouse gas emission reduction goals.
- Multiple Integrated Energy Policy Reports prepared by the California Energy Commission have evaluated the state’s ability to achieve a 33 percent RPS.
- The Renewable Energy Transmission Initiative planning group (an administration initiative involving multiple state energy and environmental agencies, public and private utilities, and environmental interests, among others) has conducted its planning work and analysis based on the assumption of the imposition of a 33 percent RPS target.
- The CPUC is moving forward with efforts to implement a 33 percent RPS with respect to the private utilities it regulates, through its Long–Term Procurement Plan process.

Budget Issues

Administration’s Spending Related to a 33 Percent RPS. Although the Legislature has not approved a budget request related explicitly to the evaluation

or implementation of a 33 percent RPS, the administration has spent significant resources for these purposes and has plans to continue this spending. The figure below summarizes these ongoing and proposed expenditures, which would total \$4 million in 2010–11 under the Governor’s budget proposal.

Administration’s 33 Percent RPS–Related Spending

(In Thousands)

	2009–10	2010–11
Air Resources Board		
Base budget	\$1,900	\$750
Proposed budget request	—	—
California Public Utilities Commission		
Base budget	\$553	\$423
Proposed budget request	— ^a	1,800
Totals	\$2,453	\$2,973

a Budget request for \$322,000 was denied by the Legislature.

The ARB estimates that it will spend \$1.9 million (from the Air Pollution Control Fund) in the current year and \$750,000 in the budget year to develop RPS–related regulations pursuant to the Governor’s executive order and the AB 32 Scoping Plan. No specific funding requests for this purpose have been submitted to the Legislature for the budget year. For CPUC, the *2009–10 Governor’s Budget* proposed a \$322,000 increase for the commission to begin the process of implementing a 33 percent RPS. The Legislature denied this budget request, finding that the proposal was premature, pending enactment of the enabling legislation to establish the 33 percent RPS. However, the CPUC has continued to conduct planning and analysis for a 33 percent RPS, and estimates that it will spend \$553,000 (from the Public Utilities Reimbursement Account) in the current year for this purpose (\$423,000 for staff costs and \$130,000 for consulting fees).

The CPUC plans to spend \$423,000 for staffing costs for these same purposes in the budget year from its existing budget resources. In addition, the Governor’s budget includes requests totaling \$1.8 million (from the Public Utilities Commission Utilities Reimbursement Account [PUCURA]) for CPUC to implement a 33 percent RPS in 2010–11. These requests include \$800,000 for seven personnel–years in staffing to implement a 33 percent RPS, and \$1 million annually (for each of the next five years) to contract for RPS program evaluation and technical assistance.

Administration’s Spending Plans Are Problematic. The administration’s spending plans discussed above are problematic for a couple of reasons. First and foremost, the expenditures by CPUC and ARB to develop RPS–related

regulations are premature given the current statute authorizing a 20 percent RPS. This regulatory activity should not occur until or unless the Legislature enacts a 33 percent standard, and only then should be implemented in a fashion consistent with any policy parameters for a revised RPS that have been established by the Legislature.

The ARB's expenditures to develop a higher RPS are particularly problematic. This is because the ARB is delving into a subject matter—renewable energy procurement—that is both outside its area of statutory responsibility and outside its area of technical expertise. The ARB is spending significant funding to work with CPUC to come up to speed on the subject matter of renewable energy procurement. In our view, this is an inefficient use of state resources. These ARB activities also constitute an inappropriate duplication of effort, given that CPUC plans to move ahead at the same time to implement a 33 percent RPS that would apply to the entities that it regulates.

Analyst's Recommendations. Given that the administration's spending plans are both premature and an inefficient and duplicative use of resources, we recommend that the Legislature take the following actions to remedy this situation. Specifically, we recommend that the Legislature:

- Deny CPUC's budget request for an additional \$1.8 million (from PUCURA) for RPS-related activity in the budget year.
- Reduce CPUC's PUCURA appropriation (Item 8660-001-0462) by an additional \$423,000—the amount the commission anticipates spending from its base budget to implement a 33 percent RPS in the budget year.
- Reduce ARB's Air Pollution Control Fund appropriation (Item 3900-001-0115) by \$750,000—the amount the board anticipates spending from its base budget to develop a renewable energy standard regulation in the budget year.
- At budget hearings, specifically direct CPUC and ARB to immediately cease spending funds for the purpose of developing a new renewable energy standard or similar requirement absent the enactment of legislation that authorizes such activities.

Staff Comments. On March 18, 2010, the Committee agreed unanimously with the findings of the Legislative Counsel and the LAO that the Governor has overstepped his authority in ordering the Administration to pursue what amounts to a 33-percent RPS. As a result, the Committee adopted the LAO recommendation and reduced the ARB budget accordingly. At that time, the Chair noted to the head of the ARB that the cessation of work on a 33-percent RPS, would go a long way toward allowing both parties to continue to negotiate an agreement (via a policy bill) in good faith. However, in the interim, staff is unaware of any such move toward accommodation by the Administration. As such, the staff recommendation will be to adopt the LAO recommendation as it pertains to the PUC.

Staff Recommendation: ADOPT the LAO recommendation on the PUC by: (1) denying the \$1.8 million augmentation requested for FY 2010-11; and (2) reducing the PUC's base budget by \$423,000 (Item 8660-001-0462). Additionally, again DIRECT the PUC and the ARB to cease spending funds for the purpose of developing a renewable energy standard or similar requirement absent the enactment of legislation that authorizes such activities.

VOTE:

2. BCP-3: Provide Staffing to Evaluate Advanced Energy Storage (AES). Many of the renewable energy resources available to California to meet its greenhouse gas reduction and RPS goals provide only intermittent electricity (e.g. when the sun is shining or the wind is blowing). However, this may not coincide with the timing of demand, and so an efficient and cost-effective means of storing energy would obviate the need to continue investing millions of dollars in infrastructure that is only needed when wind and solar production drops suddenly or when demand is peaking.

AES includes a variety of versatile resources that can help to integrate intermittent renewables into the grid by providing ancillary services such as emergency backup, generation (spinning reserve), and storage of off-peak generation for use at peak hours. Some examples of AES include: advanced batteries; pumped hydroelectric storage (that is, pumping water from a lower to a higher reservoir at night and reversing this process during the day, with the pump then being used as a turbine and the motor as a generator); and compressed-air energy storage (pumping air into a suitable enclosure where it is stored at high pressures and can later be used to drive turbines and generators).

Governor's Budget. The Governor requests three positions and \$310,000 (PUCURA) to evaluate the cost effective use of AES in support of various California policy goals, but primarily the RPS and AB 32.

Staff Comments. The PUC notes that the value of a particular AES resource will depend heavily on its location and application, and in the current policy environment, it may be difficult or impossible for an AES owner to capture all of the benefits that an AES facility can provide, thus creating a disincentive to investment. The PUC indicates that there is emerging interest (e.g., from PG&E) in large-scale storage technology, and proposes to use the requested resources to address issues related to large-scale and small-scale storage technologies, in a variety of applications and ownership structures, in order to better inform policies that provide proper incentives for AES owners and developers.

As the PUC notes, global experience with AES technologies is small. For example, there are two existing compressed-air energy storage facilities in operation worldwide. Additionally, it is unclear how much storage capacity is even needed. As a result, staff has concern that this request may be a bit premature. The Committee may wish the PUC to provide additional justification as to why the requested resources are needed now. Additionally, the Committee may wish the PUC to clarify how, and to what extent, the CEC and, particularly, the ISO, are involved in AES discussions. Staff notes that this request includes one position to serve primarily as a coordinator with state and non-state entities, but it is not clear on the state side whether other agencies are prepared to accommodate/respond to that coordination.

Staff Recommendation. DENY the request.

3. BCP-4: Bring Energy Efficiency Program Evaluation and Planning (Reimbursable Contracting Authority) On-Budget. By law, energy efficiency is the resource of first choice to meet California's growing energy demand, and investor-owned utilities (IOUs) operate various energy efficiency programs to help the state achieve its energy goals. As such, the PUC is responsible for monitoring these energy efficiency programs to ensure proper use of ratepayer funds.

Historically, the PUC has used technical consultants to perform independent evaluation and analysis of energy efficiency savings and other impacts associated with the ratepayer-funded IOUs programs and to provide technical assistance to PUC staff that oversee the evaluation of these programs. However, up until now those contracts were "off-budget." That is, while PUC staff managed the contracts, the utilities paid for the contracts directly (i.e., the contracts did not run through the PUC's reimbursable budget).

Governor's Budget. The Governor requests an increase of \$40 million in reimbursable consultant services to bring energy efficiency program evaluation, measurement, and verification (EM&V) "on-budget." Of the requested amount, \$3 million would be for technical expertise to help identify and develop energy efficiency program strategies and improvements to make existing IOU programs more effective; and \$37 million would be for technical assistance in developing, conducting, and monitoring EM&V.

Staff Comments. By allowing the PUC to contract directly for all EM&V projects, this request would reduce the potential for conflict of interest between the IOUs and the contractors who help PUC staff to monitor and evaluate the IOU's energy efficiency programs. Additionally, bringing these functions "on-budget" would promote transparency and provide the Legislature with greater fiscal oversight of the program. According to the PUC, if this proposal were to be denied, the same level of contracting would occur, but the PUC would simply not be in a position to pay for the contracts directly.

Staff Recommendation. APPROVE the request.

VOTE:

4. BCP-11: State Electricity Regulators Assistance Project (ARRA). Federal ARRA initiatives have placed additional demands on the PUC to expedite activities focused on energy efficiency, smart grid, energy storage, demand response, alternative fuel vehicles, transmission, carbon sequestration, and electric vehicles. The Energy Division advises the Commissioners and Administrative Law Judges on these topics, and there are currently approximately 50 open proceedings and more than 100 related advice letters (informal compliance filings) in this area.

The PUC applied for and received a \$1.7 million grant from the United States Department of Energy to increase administrative support of the activities identified above.

Governor's Budget. The Governor requests four limited-term positions and \$745,000 (federal funds) to provide four years of increased staffing to support the following activities:

- Address the growing number of dockets and advice letters related to ARRA electricity topical areas;
- Facilitate timely consideration of electricity dockets and advice letters including implementation and program activities related to ARRA topical areas; and
- Create additional intern positions and better train existing staff to address complex energy regulatory issues.

Staff Comments. The PUC began implementing this proposal in the current year via the Control Section 28 budget adjustment process. Staff notes no significant concerns with this request, but, given the high threshold for accountability associated with ARRA funding, wanted to be sure this item was brought to the members attention should there be any questions.

Staff Recommendation. APPROVE the request.

VOTE:

5. BCP-12: State Broadband Data and Development Grant Program (ARRA).

Increasingly, high-speed Internet access is no longer viewed as just a luxury, but as critical for economic development, education, and health care. For example, as mandated under ARRA, the Federal Communications Commission recently laid out an ambitious vision (a National Broadband Plan) for wiring the entire country with broadband in order to bring affordable, high-speed Internet connections to all Americans and make access much faster for people who already have broadband.

Last July the Governor designated the PUC as the sole entity in California eligible to apply for federal grant funding under the National Telecommunications and Information Association's (NTIA) State Broadband Data and Development Grant Program (State Broadband Mapping program). The PUC received \$2.4 million for two years of broadband mapping activities.

Governor's Budget. The Governor requests four limited-term positions and \$2.4 million (federal funds) to support four years of broadband mapping and planning efforts.

Staff Comments. In addition to providing the NTIA with the desired broadband data regarding availability, speed, and infrastructure for every broadband service provider, the PUC indicates the data collected under this proposal will be utilized to create a statewide, interactive broadband map that will be available to the public (via the Internet). This mapping effort will inform state policymakers in efforts to eliminate the digital divide.

The PUC began implementing this proposal in the current year via the Control Section 28 budget adjustment process. Staff notes no significant concerns with this request, but, given the high threshold for accountability associated with ARRA funding, wanted to be sure this item was brought to the members attention should there be any questions.

Staff Recommendation. APPROVE the request.

VOTE:

6. Staff Issue: Landlords Charging Exorbitant Rates for Drinking Water in Certain Coachella Valley Communities. Last week in a discussion of the Department of Water Resources budget (April 22, 2010), the Committee heard a staff issue involving drinking water quality for a number of the unincorporated communities in the Coachella Valley (including Mecca, Thermal, and Oasis). It has come to staff's attention that, in addition to the health concerns posed by the level of naturally-occurring arsenic in the well water in that region, many members of these communities are being charged exorbitant rates by their water providers (e.g., the mobile home park owner) for the pumping of arsenic-laced water. For example, a number of residents have received monthly water bills in excess of \$500.

The PUC investigates water and sewer system service quality issues and analyzes and processes utility rate change requests. Additionally, the PUC works directly with utility management to track and certify compliance with PUC requirements. The PUC's objectives in regulating water utilities rest on four key principles: 1) safe, high quality water; 2) highly reliable water supplies; 3) efficient use of water; and 4) reasonable rates and viable utilities.

Staff Comments. It has come to staff's attention that in at least one instance, dating to June 2009, a community resident filed a complaint with the PUC. The defendant made a filing in November 2009, but the issue is still awaiting a PUC ruling. Therefore, the Committee may wish to inquire as to status of the complaint, and, in particular, when the resident(s) can expect a ruling.

Staff Recommendation: Informational only at this time.

8570 Department of Food and Agriculture

The California Department of Food and Agriculture (CDFA) provides services to both producers and consumers of California's agricultural products in the areas of agricultural protection, agricultural marketing, and support to local fairs. The purpose of the agricultural protection program is to prevent the introduction and establishment of serious plant and animal pests and diseases. The agricultural marketing program promotes California's agricultural products and protects consumers and producers through the enforcement of measurements, standards, and fair pricing practices. Finally, the department provides financial and administrative assistance to county and district fairs.

Governor's Budget. The Governor's Budget includes \$377 million (\$130 million GF) for support of the CDFA, an increase of approximately \$38 million, due primarily to increased efforts to control and eradicate various agricultural pests (supported by increased industry assessments as well as federal funds).

ITEMS PROPOSED FOR VOTE-ONLY

1. BCP-1: Mitigate the Spread of the Asian Citrus Psyllid (ACP). The Governor requests 38 one-year limited-term positions, 117 temporary help positions, and \$19.8 million (federal funds) to fund detection and quarantine to prevent the spread of the ACP in California. These efforts to protect the million-dollar California citrus industry are supported by the United States Department of Agriculture (USDA).

2. BCP: California Citrus Pest and Disease Prevention Committee (Implement AB 281). The Governor requests seven positions and \$15 million (Agriculture Fund) to implement the California Citrus Pest and Disease Prevention Committee created pursuant to Chapter 426, Statutes of 2009 [AB 281, DeLeon]. This legislation was passed largely in response to the threat posed by the ACP (see Item 1 above) and the requested funding would be supported by an industry-approved assessment.

3. BCP: Citrus Nursery Stock Pest Cleanliness Program (Implement SB 140). The Governor requests two positions and \$250,000 (Agriculture Fund) to establish a Citrus Nursery Stock Pest Cleanliness Program to protect citrus nursery source propagative trees from diseases, pests, and other risks and threats. The requested expenditure would be supported by a new assessment on the industry.

4. BCP-3: Relocation and Consolidation of Programs: Annex Building and Westfield Downtown Plaza. The Governor requests a one-time augmentation of \$4.6 million (various funds) and an ongoing augmentation of \$116,000 to support the costs associated with the relocation of CDFA staff that is currently located in the Annex Building at 1215 O Street and at the Westfield Downtown Plaza at 560 J Street. The O Street facility was ordered vacated due to lack of fire and safety protection and the

Westfield Downtown Plaza has been subject to repeated burglaries (to which the building management has failed to adequately respond).

5. BCP: Fertilizing Materials: Organic Input Material (Implement AB 856). The Governor requests three positions and \$416,000 (Agriculture Fund) to monitor input material production processes at fertilizing material manufacturing facilities, consistent with Chapter 257, Statutes of 2009 [AB 856, Caballero], in order to ensure that “organic” foods are truly organic (and are not tainted by use of “non-organic” input materials in fertilizer).

6. BCP: Municipal Shelter Spay-Neuter Fund (Implement AB 2291). The Governor requests \$194,000 (Municipal Shelter Spay-Neuter Fund) to distribute, consistent with Chapter 328, Statutes of 2008 [AB 2291, Mendoza], grants to eligible municipal shelters for the purposes of providing low cost or free spay-neuter services. The grants are to be supported out of approximately \$196,000 in contributions to the above-named fund from voluntary contributions designated on the 2008 California Tax Return.

7. BCP-2: Continue Support of Board of Equalization (BOE) Tax Enforcement Program. The Governor proposes to make permanent an existing pilot project in which CDFA personnel at the Needles (I-40) border protection stations inspect cargo, photocopy pertinent documents, and pass along potential leads to the BOE for collection of use tax. In FY 2008-09 the project resulted in \$14.3 million in GF revenue, and the Administration anticipates similar revenue on an ongoing basis with the continuation of the program. To this end, the Governor requests three positions and \$244,000 (\$232,000 ongoing) in reimbursement authority (so that the CDFA can expend GF support provided by the BOE through an interagency agreement).

Staff notes that this item conforms to a related request in the BOE budget.

8. BCP-7: Expand the BOE/CDFA Tax Enforcement Program to Three Additional Stations. The Governor requests nine positions and \$706,000 (reimbursement authority) to expand the BOE/CDFA Tax Enforcement Program (see description above in item 2) to three additional border protection stations (Yermo, Truckee, and Hornbrook). The Administration estimates the requested resources would generate an estimated \$44.4 million increase in annual GF revenue.

Staff notes that this item conforms to a related request in the BOE budget.

Staff Recommendation (for Vote-Only Items 1-8): APPROVE the requests (1-8) listed above.

VOTE:

ITEMS PROPOSED FOR DISCUSSION

BCP-5: Add Staff to State Board of Food and Agriculture. The State Board of Food and Agriculture (Board) consists of 15 members, appointed by the Governor, who each represent and further the interest of a particular portion of the agricultural industry. The Board acts as a consultative and policy body for farmers and consumers, and is empowered by law to investigate the needs of the agricultural industry and the functions of the CDFA in relation to such needs, and to confer and advise the Governor and the Secretary (of the CDFA) on how the agricultural industry and the consumer of agricultural products may best be served by the CDFA.

Governor's Budget. The Governor requests three positions and \$513,000 (Agriculture Fund). According to the CDFA, these positions would help the Board address critical environmental, community, and business issues, complex regulations, and conflicting priorities that confront 75,000 California farmers and ranchers and threaten the state's \$37 billion agricultural economy.

Staff Comments. The CDFA notes that although the Board is authorized in statute to "make investigations, conduct hearings, and prosecute actions concerning all matters and subjects which are under jurisdiction of the department," the Board does not have its own administrative staff. Accordingly, the Board is seeking the requested positions so that it may more effectively and efficiently represent consumers, farmers, and ranchers on critical issues such as climate change; water supply, reliability, and quality; air quality; alternative energy; public health, invasive species, wildlife habitat, and animal welfare; and forging alliances. For example, CDFA staff indicate these positions would help deliver "ground-truths" to the California Environmental Protection Agency, the Natural Resources Agency, the California Emergency Management Agency, the Department of Health and Human Services, and the Labor and Workforce Development Agency.

Staff notes concern with the lack of justification for the requested resources insofar as it is unclear that the three requested positions would provide significant added value given that many of the "critical issues" identified above already have very public/transparent regulatory and rulemaking processes (e.g., air quality, water quality, and climate change) that require the diverse opinions and interests of the state, including the agricultural community, are considered. Additionally, the CDFA has not adequately demonstrated that there is a "problem"—that is, that these existing processes have failed to incorporate the views and needs of farmers and ranchers into the policy-making process. The Committee may wish to request the CDFA to further clarify its justification in this respect; however, in the absence of additional, and compelling, information, and in light of the Committee's general prejudice against expanding the state payroll during the ongoing fiscal crisis, staff recommends this request be denied.

Staff Recommendation: DENY the request.

VOTE:

3540 Department of Forestry and Fire Protection

The California Department of Forestry and Fire Protection (DFFP), under the policy direction of the Board of Forestry, provides fire protection services directly or through contracts for timberlands, rangelands, and brushlands owned privately or by state or local agencies. In addition, DFFP: (1) regulates timber harvesting on forestland owned privately or by the state and (2) provides a variety of resource management services for owners of forestlands, rangelands, and brushlands.

DISCUSSION ITEM

Staff Issue: Funding and Fiscal Oversight of Fire Prevention and Fire Protection Expenditures.

Background. DFFP “fire protection” involves activities directly related to fighting an active fire, while “fire prevention” includes any number of activities aimed at reducing or eliminating the risk of a fire starting—including mechanical fuel reduction, prescribed burns, and defensible space inspections.

The proposed FY 2010-11 DFFP fire protection budget is approximately \$1 billion (including \$523 million GF—counting both base budget and Emergency Fund [E-Fund] resources—and another \$200 from the Governor’s proposed Emergency Response Initiative homeowner’s insurance surcharge—which would have to be backfilled by GF if it fails to gain sufficient votes [as it did last year]).

By comparison, the proposed DFFP fire prevention budget contains \$21 million (including \$18.6 million GF).

Fire protection costs continue to rise, due in no small part to increased development in the wildland urban interface and the concomitant need to protect life and property from wildfires in these areas, and the DFFP’s increasing role in the state as an all-purpose emergency response agency. Given the state’s ongoing fiscal woes and the fact that fire protection and prevention costs are predominately borne by the GF, it is worth investigating whether fiscal oversight is adequate and whether each dollar is being spent optimally.

Staff Comments. In the stead of a lengthy staff write-up, the LAO will provide a hand-out that will frame several items for the Committee’s consideration and provide various recommendations. These items include:

- **E-Fund** – The DFFP E-Fund is intended to pay large incident fire-fighting costs. Is this reflected in the Governor’s Budget? Does the Legislature currently have adequate oversight of E-Fund expenditures?
- **Fire Protection v. Fire Prevention** – “An ounce of prevention is worth a pound of cure.” Are we currently budgeting the right amounts for fire protection and fire prevention, or is there a more optimal allocation of scarce GF?

- **Defensible Space Inspections** – When the Legislature signed-off on a 2006 memorandum of understanding to approve year-round staffing and the extension of the firefighter workweek, the expectation was that increased DFFP staffing would lead to increased defensible space inspections in the off-peak season. Has this occurred, and have these additional staff hours been maximized to prevent fires during the rest of the year? (Staff notes that the DFFP has not yet submitted the statutorily required fire prevention report that was due on January 1, 2010.)
- **Schedule A Agreements** – The DFFP commonly contracts with local government for the department to provide local fire protection and emergency services. Is the state receiving fair compensation for these agreements?

Staff Recommendation: Request LAO, DOF, and DFFP to work with staff to formulate a set of actions, for adoption at a future hearing, that will improve legislative fiscal oversight of the DFFP fire protection and fire prevention activities and better optimize the expenditure of limited GF resources.